

Markets This Week Ahead of the Open

Key Takeaways

- Equities remain weighed down, as the Dollar and Yields appreciate
 - In line with market expectations, the Federal Reserve keeps rates steady
 - Sentiment has shifted from expectations of steady Fed policy to the potential for a more restrictive stance
 - The ongoing conflict with Iran continues to remain the focal point across markets
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This past week equities and broad market indexes continued to remain down as investors came to terms with a “higher-for-longer” Fed, and economic data that further amplified inflationary concerns.

This week saw the release of the BLS’s monthly PPI report alongside the Federal Reserve’s second FOMC meeting of the year. The PPI report, which tracks prices paid to producers for intermediate and final goods, showed continued strong price increases. This data, which is typically seen as a leading indicator of consumer inflation, further amplified ongoing inflationary concerns. Following the report, equities and metals edged lower, while yields and the dollar advanced.

Directly after this report came the Fed’s second FOMC meeting, in which it held rates steady in line with market expectations. In regard to this meeting, investor focus wasn’t necessarily on the policy decision that had been made, but rather on the factors that were highlighted and what the Fed continues to monitor. Elevated inflation, a weakening labor market, and the conflict with Iran were the main catalysts that had been outlined.

Within the FOMC, the decision to hold rates was uniform across the board, outside of one dissent by Stephen Miran. It is important to note that Christopher Waller, who had advocated for a rate cut in the prior meeting, was in favor for holding rates this time around. As of recently the Fed has faced complications in achieving its dual mandate due to the ongoing complications of the Iranian conflict. Concern remains, in particular, over the surge in oil prices and its potential to structurally elevate inflationary pressures. Any prolonged increase in oil prices would not just lead to this, but potentially even slower economic growth. A rate cut later in the year was still signaled in this past meeting, but for now, rates remained steady.

Markets, on the other hand, had reacted adversely to this month’s meeting. The reactionary price action of yields and equities took the headlines, but a shift in investor sentiment was overlooked. Prior to this meeting, expectations were centered around the Federal Reserve maintaining its current policy stance, but after this expectations shifted. Some traders have begun pricing in the potential for rate hikes, while economists at Bank of America signaled the possibility of this as well. Around a month ago, expectations surrounding a dovish Fed were prevalent given a slowing labor market, and cooling inflation, but now this notion seems remote.

The conflict within Iran continues to be the driving force behind the price action and sentiment we've seen in markets these past three weeks. In particular, what continues to be the focal point is the elevation in oil prices, and what this could mean further down the line. Investors continue to rotate out of equities and emerging markets, further prolonging the market's current risk-off episode. Any signs of further escalation within the Middle East would advance this current environment, and any capital situated within equities could be materially impacted. For now, the ongoing rotation out of risk assets and metals continues to remain the central theme, as more investors continue to adopt a defensive strategy.